

This record is a partial extract of the original cable. The full text of the original cable is not available.

UNCLAS SECTION 01 OF 02 TAIPEI 003992

SIPDIS

STATE PLEASE PASS AIT/W AND USTR

STATE FOR EAP/RSP/TC, EAP/EP AND EB/IFD/OIA

USTR FOR SCOTT KI

USDOC FOR 4420/USFCS/OCEA/EAP/LDROKER
USDOC FOR 3132/USFCS/OIO/EAP/ADAVENPORT

TREASURY FOR OASIA/ZELIKOW AND WISNER

TREASURY PLEASE PASS TO OCC/AMCMAHON

TREASURY ALSO PASS TO FEDERAL RESERVE/BOARD OF
GOVERNORS, AND SAN FRANCISCO FRB/TERESA CURRAN

E.O. 12958: N/A

TAGS: [EINV](#) [EFIN](#) [ECON](#) [TW](#)

SUBJECT: Taiwan Growth Slowing

SUMMARY

1. Taiwan's economic growth is expected to drop from 7.3 percent in the first half of 2004 to 4.7 percent in the second half following declines in export growth, industrial production, and private investment. END SUMMARY.

Economic Slowdown

2. In late November 2004, the Directorate General of Budget, Accounting and Statistics (DGBAS) adjusted Taiwan's estimated 2004 economic growth upward for the fifth time to nearly six percent. At the same time, DGBAS predicted Taiwan's economic growth would slow from 7.3 percent in the first half of 2004 to 4.7 percent in the second half and further down to 4.5 percent in the second half of 2005.

3. Tsai Hung-kun, Deputy Director of the DGBAS' Statistics Bureau, attributed Taiwan's economic slowdown mainly to three factors: rising interest rates and oil prices and the "negative wealth effect" of falling stock prices. The U.S. Federal Reserve Board's raising interest by one percentage point during June - October dampened lowered demand for Taiwan's exports. Higher oil prices pushed up prices and dampened Taiwan consumer spending in Taiwan. A decline in Taiwan stock prices in the third quarter of 2004 reduced the wealth of local consumers, and further weakened their confidence and demand.

Export and Import Growth Down

4. According to DGBAS, export growth in 2004 declined from 29 percent in the second quarter to 21 percent in the third quarter and will fall to an estimated 12 percent in the fourth quarter. Deputy Director Tsai projected that export growth would drop to seven percent in 2005. He predicted import growth would slow from 40 percent in the second quarter to 19 percent in the fourth quarter of 2004 and down to six percent in 2005.

Orders Filled by Offshore Production Bases

5. However, the growth of export orders has not declined along with the decline in growth of exports. This reflects the fact that Taiwan offshore production factories fill an increasing percentage of export orders received by Taiwan companies. According to a Ministry of Economic Affairs (MOEA) survey, export orders have grown at a year-on-year rate of 26 percent for the first ten months of 2004. A survey by the Ministry of Economic Affairs showed that Taiwan business firms filled nearly 40 percent of the export orders by shipments from overseas production factories and that 60-70 percent of those shipments came from China.

Strong Competition from South Korea

6. According to MOEA officials, strong competition from South Korea is eroding Taiwan business firms' market in China, particularly in the high-tech area. Demand from Taiwan-invested down-stream flat panel display firms in China contributed to triple-digit growth in Taiwan's exports of flat panels and related products to China in the first half of 2004. However, according to MOEA, South Korean competitors have successfully snatched a large share of this market in China by undercutting Taiwan prices on these

products. As a result, Taiwan's exports of flat panel products posted a decline from 140 percent growth in the first seven months to 86 percent in August and 20 percent in September 2004. South Korea replaced Taiwan as the second largest source of China's imports in September 2004.

Investment and Money Supply Growth Decline

17. Slower export growth in the second quarter was reflected in rising inventories in the fourth quarter and a drop in private investment growth from 33 percent to 20 percent. DGBAS predicts private investment growth in 2005 would slip to nine percent. Industrial growth dropped from 14 percent in the first quarter and 15 percent in the third quarter to three percent in October 2004. Another indication of economic slowdown is declining money supply growth. M1B growth in October 2004 at 14.7 percent was the lowest in 14 months. Growth in M2 plus bond funds also hit a 12-month low of 6.3 percent. (M1B is a measure of money that refers primarily to money that can be used in transactions. M2 is a broader measure of money that includes M1B plus deposited money that cannot be readily used in transactions.)

Lowest Unemployment in Three Years

18. Despite the economic slowdown, Taiwan's unemployment rate in October 2004 declined to 4.3 percent, the lowest rate in three years and down from 5.3 percent in August 2002 and the lowest rate in three years.

Manufacturing Firms: Pessimistic

19. An October 2004 survey showed that only 13 percent of Taiwan businesses expect business performance to improve over the coming three months, down from over 33 percent in January and February 2004.

KEEGAN